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DHHS Contracting for Cost Shared Non-MaineCare Human Services — Cash Management Needs Improvement to Assure Best Use of Resources, 2008

Maine State Legislature

Office of Program Evaluation and Government Accountability

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Performance
Audit

FINAL
REPORT



DHHS Contracting for Cost Shared Non-MaineCare Human Services — Cash Management Needs Improvement to Assure Best Use of Resources

Report No. SR-CHSS-07

a report to the
[Government Oversight Committee](#)
from the
[Office of Program Evaluation & Government Accountability](#)
of the Maine State Legislature

July
2008

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OPEGA is an independent staff unit overseen by the bipartisan joint legislative Government Oversight Committee (GOC). OPEGA's reviews are performed at the direction of the GOC. Independence, sufficient resources and the authorities granted to OPEGA and the GOC by the enacting statute are critical to OPEGA's ability to fully evaluate the efficiency and effectiveness of Maine government.

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EXECUTIVE SUMMARY

DHHS Contracting for Cost Shared Non-MaineCare Human Services — Cash Management Needs Improvement to Assure Best Use of Resources

OPEGA focused on the financial close-out phase of cost shared non-MaineCare human services contracts.

OPEGA estimates DHHS could improve cash flow by \$2.6 million annually through enhanced cash management. In addition, assertive collection efforts could realize a one time infusion of \$960,660.

DHHS needs to better balance financial management and service delivery. This is being addressed as part of the Department's ongoing transformation, but additional work remains.

The Maine Legislature's Office of Program Evaluation and Government Accountability (OPEGA) has completed a performance audit of contracting for human services at the Department of Health and Human Services (DHHS). OPEGA conducted this audit at the direction of the joint legislative Government Oversight Committee (GOC), in accordance with 3 MRSA §§991-997 and the Government Auditing Standards set forth by the United States Government Accountability Office.

The Department reported planned expenditures of approximately \$187 million in fiscal year 2007 and \$185 million in fiscal year 2008 for agreements with community based agencies for delivery of human services. This review focused on identifying potential General Fund opportunities related to the financial close-out phase of a specific group of these agreements: cost shared non-MaineCare agreements for human services.

OPEGA has concluded that there are opportunities associated with the agreements reviewed. We conservatively estimate that improving cash management practices for cost shared agreements could result in DHHS retaining approximately \$2.6 million annually that may otherwise have been overpaid to providers and could instead be used immediately to support other services. Assertive collection efforts could produce faster collection of future overpayments and result in a one time infusion of \$960,660 from full collection of balances already owed.

Specific findings noted in this report include the following:

- Cash management was inadequate and resulted in providers owing balances back to the State.
- Collections of amounts due to the State were not timely.
- Financial data for decision makers was lacking, but recent improvements have been made and more are planned.
- Appeals of cost settlements consume resources and may be avoidable.

The Department acknowledges its fiscal stewardship role and has been working, since early 2007, on a financial transformation plan. OPEGA observed that culture change is needed at DHHS to better balance fiscal management and service delivery and to bridge the historical gap between the Department's program and financial staff. This culture change has been part of DHHS' transformation plan, but significant challenges remain and must be addressed if the transformation is to be successful.

FULL REPORT

DHHS Contracting for Cost Shared Non-MaineCare Human Services — Cash Management Needs Improvement to Assure Best Use of Resources

Purpose

Many human services are provided by DHHS through agreements with community based agencies.

DHHS reported \$185 million in FY 2008 contract encumbrances for human services, of which \$85 million was General Fund.

The Maine Legislature's Office of Program Evaluation and Government Accountability (OPEGA) has completed a performance audit of contracting for cost shared non-MaineCare human services at the Department of Health and Human Services (DHHS). OPEGA conducted this audit at the direction of the joint legislative Government Oversight Committee (GOC), in accordance with 3 MRSA §§991-997 and the Government Auditing Standards set forth by the United States Government Accountability Office.

DHHS' mission is to provide integrated health and human services to the people of Maine to assist individuals in meeting their needs. Human services are provided to citizens both directly by the Department and through agreements with community based agencies. These agreements are a significant and essential part of DHHS' service delivery system.

The Department reported a total of approximately \$187 million in agreement encumbrances for human services contracted with community based agencies (referred to throughout this report as "providers") for fiscal year 2007 and \$185 million for fiscal year 2008.¹ Table 1 shows a breakdown of these amounts by fund. Actual expenditures on payments to providers likely exceed these encumbered amounts (encumbered funds are funds set aside for a specific future use that may not be expended on other transactions).

Table 1. DHHS Agreements with Community Based Agencies by Fund and Fiscal Year

Fiscal Year	General Funds	Federal Funds	Other Funds*	Total Encumbrances
2007	\$74 million	\$90 million	\$23 million	\$187 million
2008	\$85 million	\$78 million	\$22 million	\$185 million

*Other funds include Special Revenue and Fund for Healthy Maine.

Source: DHHS Annual Reports on Services Contracted with Community Based Agencies for Fiscal Years Ending June 30, 2007 and June 30, 2008.

¹ See Appendix A for statutory (34-B MRSA §1208) definitions of agreements, human services and community agencies. These figures do not include services provided through MaineCare.

OPEGA sought opportunities for savings and efficiencies in the financial close-out phase of cost shared non-MaineCare human services agreements.

Legislators have raised a variety of questions and concerns regarding DHHS contracting over the last several years, any of which could constitute a specific audit in its own right. At the time the scope for this audit was established, the State was seeking to resolve a structural budget gap and the GOC was most interested in identifying opportunities for improving the State's financial condition, particularly the condition of the General Fund.

As directed by the GOC, OPEGA initially set out to determine whether there were opportunities for cost savings or improved efficiency in DHHS' contracting processes for health and human services. It became clear, however, that producing a timely result for the Legislature required narrowing the scope for this audit. Our preliminary research had identified potential General Fund opportunities related to the financial close-out phase of cost shared non-MaineCare human services agreements. Consequently, we focused the remainder of our work in that area.

In February 2008, OPEGA presented an interim memo to the GOC on the fiscal opportunities identified as a result of our work to date. See Appendix B for that memo and DHHS' response. This final report discusses more fully the root causes and other issues surrounding those fiscal opportunities.

Methods and Scope

In performing this audit, we gained a general understanding of DHHS' contracting processes and related issues by:

- surveying 173 DHHS staff involved in the Department's contracting processes and reviewing the 81 responses;
- interviewing key employees of DHHS and the Department of Administrative and Financial Services (DAFS);
- documenting contracting processes;
- reviewing reports from similar audits in other states; and
- reviewing State Single Audit Reports from the State Auditor.

OPEGA reviewed contracting processes and examined in detail the cost settlements for a sample of 28 providers.

For detailed review, we judgmentally selected a sample of providers that appeared to have large General Fund encumbrances. This sample included 28 providers out of the 381 providers considered to be auditable by DHHS' Division of Audit². Because the Department is currently settling agreements about two years after they end, in order to review agreements that had already been through the settlement process we selected agreements mostly from State fiscal year 2004.

² The DHHS Division of Audit does not audit all providers with cost-sharing contracts. For example, cost-settlements are not performed on providers with less than \$25,000 in cost-sharing contracts.

For the 28 providers in our sample we:

- reviewed the financial settlement audit report and supporting documentation prepared by the DHHS Division of Audit;
- analyzed associated appeals filed by providers, and the results of those appeals; and
- investigated subsequent collection of amounts the Division of Audit found due to the State.

Background

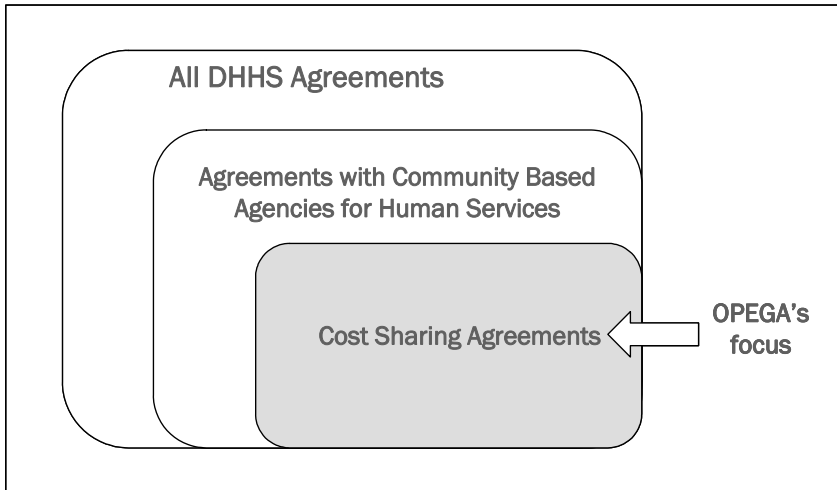
Overview of Agreements Used by DHHS to Purchase Human Services

DHHS purchased service agreements may take a variety of forms. This review focused on the cost shared type.

Purchased service agreements may take many forms, such as fee for service, where DHHS pays the provider an agreed upon fee per unit of service, and cooperative agreements, which involve joint participation between the Department and the University of Maine to both provide services to the people of the State and further the teaching, research, and public service missions of the University. Table 2 provides brief descriptions of the basic agreement types.

Table 2. Descriptions of Basic Agreement Types

Cost Shared	Agreement where the percentage of net allowable expenses is based on a program budget and the Department's portion of allowable expenses of the total program.
Fee-for-Service	Agreement based on rate setting criteria such as MaineCare rates, market rate study, rates imposed by State and Federal statute, or negotiated rates.
Unit Cost	Agreement based on a program budget where the amount of available funds from the Department is divided by the Department's share of total program units to arrive at the unit cost.
Line Item Expense	Agreement where Department funds are earmarked for specific cost items within the total program budget and may not be used for any other expense items in the budget.
Open Payment/Invoice	Agreement where funds are earmarked for specific deliverables outlined in the agreement for a particular project.
Cooperative Agreements	Agreement involving joint participation between the Department and the University of Maine to both provide services to the people of the State and further the teaching, research, and public service missions of the University.

Figure 1. OPEGA's Focus Within DHHS' Contracting Activities

This audit focused on the Department's cost shared agreements. For these agreements, DHHS agrees to cover a certain percentage of the provider's costs for expenses allowed under the agreement's guidelines or applicable federal regulations. Instead of being paid per unit (such as per person served or per day of service), providers with cost shared agreements are paid enough to cover allowable costs as stated in the agreement, regardless of whether they serve 1 or 1,000 people. These agreements are not supposed to result in a profit for the provider, unlike fee for service agreements which pay a set fee per unit regardless of the

underlying costs and may result in a profit or loss for the provider. DHHS had 834 active cost shared agreements with 392 community based agencies during SFY 2008 with a combined encumbered amount of about \$139 million.

General Overview of DHHS' Agreement Administration Processes

The need for contracted services is generally determined by one of DHHS' program offices.

All agreements are required to be reviewed and approved by both the DHHS Division of Purchased Services and the DAFS Division of Purchases.

DHHS' process for establishing, monitoring, settling, or auditing agreements for human services varies depending on the program office managing the agreement and on the type of agreement; however, at a high level the process flow is somewhat standard. Figure 2 provides a high-level overview of the process.

Generally, the need for contracted services is determined by one of DHHS' program offices. Once a need is identified, each agreement goes through a development phase, which may consist of an RFP process if the agreement is to be bid out. During the development process DHHS' program staff establish the budgetary and performance requirements for the agreement. DHHS' Division of Purchased Services (DPS) is also involved at this stage, and may provide more or less assistance with agreement development depending on the program office that is contracting for services³.

DHHS Program Offices

- Office of Adult Mental Health Services
- Office of Substance Abuse Services
- Office of Adults with Cognitive and Physical Disability Services
- Office of Child & Family Services
- Office of Multicultural Affairs
- Maine Center for Disease Control & Prevention
- Office of Elder Services
- Office of Integrated Access and Support
- Office of MaineCare Services
- Division of Licensing and Regulatory Services
- Office of Quality Improvement

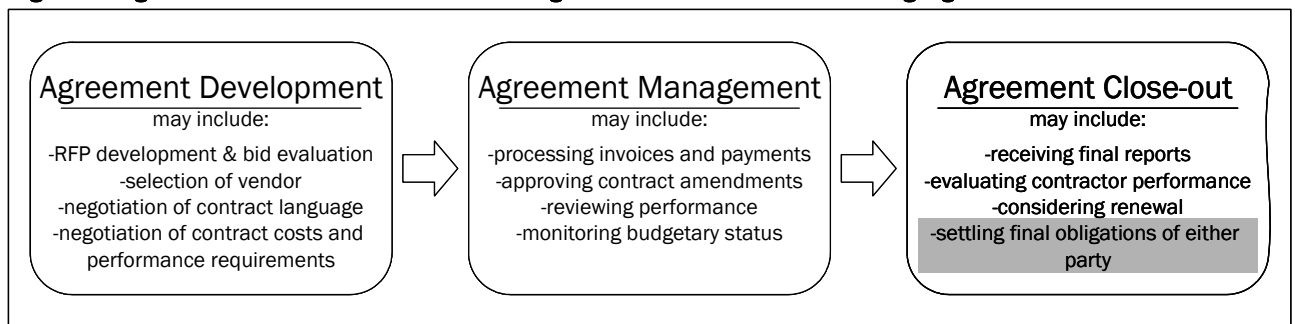
³ DHHS' Division of Purchased Services offers a range of contract management services to DHHS program offices, ranging from assistance with development of contract language to monitoring contract utilization or authorizing payments based on contracts. Some DHHS program offices make full use of these services, while others use much less.

When they end, each cost shared agreement undergoes a final settlement process. This process was the focus of OPEGA's review.

All of DHHS' agreements for human services are required to be reviewed and approved by both DPS and the DAFS Division of Purchases. During the life of the agreement, performance may be monitored by DHHS program staff and payments may be authorized by either program staff or DPS. Again, the level of DPS involvement depends on the program office responsible for the agreement.

When they end, agreements for human services undergo a close-out or final settlement process. This may include delivery of final reports required under the agreement terms and/or a financial settlement to ensure that the dollars paid during the agreement's life have been appropriate and allowable. Any remaining balances owed to either party should be resolved at this time. This financial settlement portion of the close-out phase was the focus of OPEGA's review.

Figure 2. High-Level Overview of DHHS' Contracting Process with OPEGA's Focus Highlighted



Detail of DHHS' Financial Settlement Processes for Cost Shared Agreements

Final cost settlement for DHHS' agreements is performed by the DHHS Division of Audit. Most agreements are currently settled about two years after they end.

Prior to the start of a cost shared agreement, the provider presents a proposed budget for the services in question. DHHS uses the budget to calculate how much it will agree to pay the provider. That amount is then paid out in pre-determined periodic installments over the course of the agreement period with adjustments for unplanned but allowable expenses made as necessary. Within 90 days of the end of the agreement period, the provider is supposed to submit a final financial statement showing actual costs for allowable expenses and actual payments received from DHHS. This statement should indicate whether the provider has received more than needed, or not enough, during the agreement period.

After the agreement's end most providers will be required to get an independent financial audit as one of the agreement requirements. This audit usually must occur within 9 months of the provider's fiscal year end. It examines such things as allowability of costs and cost allocation among various grants in great detail, and may result in financial statements, supplemental schedules and findings for the provider. The documents produced by the independent auditor are reviewed as part of each cost shared agreement's formal and final cost-settlement conducted by auditors in DHHS' Division of Audit.

Cost settlement entails reconciling each provider's allowable costs to the agreement payments they received.

Because of back-logs, most agreements currently wait approximately two years after ending before undergoing this final cost settlement. During the settlement process DHHS' own auditors review the independent auditor's report, confirm that the actual expenses submitted by the provider for cost sharing are allowable, and verify the amounts paid to the provider over the agreement's life. They then reconcile the provider's costs to the payments the provider received and determine whether any final amount is due from the provider to the State or vice versa to settle the agreement in full. The auditors also calculate interest on amounts due as necessary.

Providers may appeal the results of DHHS cost settlements if they disagree with them.

Providers may elect to contest the DHHS Division of Audit settlement through an established appeals process within the Department. Appeals are addressed first by the Division of Audit and second by DHHS upper management. Providers that are unhappy with the resolution provided by those two stages may carry their appeal to a hearing with the DHHS Division of Administrative Hearings.

After any appeals have been fully resolved there may still be a balance owed to the State. Responsibility for collecting these amounts currently falls to the DHHS Medicaid Finance Group, a group led by DHHS and made up of DAFS Service Center and DHHS staff. These collection responsibilities were previously shared, somewhat ambiguously, by the Service Center and the DHHS Purchased Services group. During OPEGA's review there were no standard procedures for collection of these amounts; however, as of the writing of this report, the Department is in the process of implementing new procedures.

DHHS' Ongoing Efforts to Improve Financial Management and Agreement Administration

DHHS' culture has historically focused heavily on service delivery, without paying adequate attention to fiscal management.

DHHS has historically had a culture focused heavily on delivery of services without paying adequate attention to the management of related finances. Over the years, the State Auditor has reported recurring findings of internal control deficiencies and noncompliance during the State Single Audit. In addition, the Department realized that it had accidentally grown into two distinctly separate branches, fiscal and program, that failed to work together. As a result, it has had limited ability to attach fiscal data to its programs.

Deloitte Reviewed DHHS' Processes for:

- planning and budget management;
- financial analysis and reporting;
- performance management and advice;
- stakeholder management;
- risk management and control;
- compliance and rate setting; and
- finance organization management.

In the fall of 2006, DHHS hired Deloitte Development LLC to evaluate its finance functions and develop a financial transformation strategy. Deloitte assessed DHHS Finance against a five stage maturity model and determined that it lay between stages one and two—characterized by a lack of performance measures, limited process documentation, communication issues, a developing organizational structure and inadequate or basic support tools. The consultant recommended a detailed 18 month plan to move the Department to stage three as characterized by established performance metrics, documented processes, formal and regular communication, clearly defined roles, and the existence of management tools to help monitor issues.

For the past year the Department has been in the process of implementing a financial transformation plan developed by a consultant hired in 2006.

The Department has been actively implementing this financial transformation plan for the past year with the goal of improving financial management practices and related culture. The pace of implementation has been affected by continuing challenges associated with the Maine Claims Management System (MECMS), the merger of former Departments of Behavioral Services and Human Services into DHHS, and the move to the Service Center model for accounting and processing services. New challenges have been presented by budget issues and adoption of the new statewide AdvantageME accounting system.

One example of the change that is occurring is a redesign of the organizational structure related to finance functions, including the 2007 creation of the Division of Program and Fiscal Coordination under the DHHS Deputy Commissioner of Finance. The new Division is intended to bridge the long-standing gap between fiscal staff and program staff.

Goal of the Office of Program and Fiscal Coordination

“getting to the point where we can clearly state that we served this many people, and it cost us this many dollars, and here are the results we achieved.”

Kirsten Figueroa
DHHS Deputy Commissioner of Finance

It encompasses the Department’s purchased services and rate setting groups and has 7 program fiscal coordinator positions. These positions are responsible for connecting DHHS program staff with the Division’s groups and the DAFS Service Center that supports DHHS. The 7 program fiscal coordinator positions have not all been filled yet, however the new Division has already delivered on one of its first goals—producing standardized financial reports that were not previously available.

Conclusions

OPEGA estimates DHHS could improve cash flow by \$2.6 million annually. Assertive collection efforts could realize a one time infusion of \$960,660.

DHHS’ contracting for cost shared non-MaineCare human services does present opportunities for improved efficiency and cash management. Current processes for these agreements have resulted in some providers being paid more than is necessary over the course of the agreement. Collection of these overpaid amounts has not always been timely and sometimes has not happened at all. Some receivables for these past due amounts have never been recorded, which makes quantifying total amounts owed to the Department difficult.

We conservatively estimate that improving cash management practices for cost shared agreements, as noted in our findings, could result in DHHS retaining approximately \$2.6 million annually that may otherwise have been overpaid to providers and could instead be used immediately to support other services. Improving collection efforts could also result in a one time infusion of \$960,660 from full collection of balances already owed and faster collections in the future⁴.

⁴ DHHS budgets to collect a certain amount of receivables each year. However, the Department is currently unable to quantify expected collections specifically associated with cost shared agreements with non-MaineCare providers. They expect to be able to produce this detailed receivable data by summer 2009.

DHHS is in the midst of a significant transformation focused on improving financial management. A successful transformation is critical to the State's financial health.

Although our findings apply only to the specific areas audited, addressing these items should also produce positive changes in other phases of DHHS' contracting process and contribute to their long term financial transformation. The Department's management acknowledges that much remains to be done but believes that significant change has already been made. OPEGA did observe examples of progress over the course of this review. Given that DHHS represents approximately 32% of the State's General Fund budget, a successful transformation is vital to the State's financial health and deserves active oversight and support from both the Administration and the Legislature as it progresses.

Findings and Observations

Finding 1 - Inadequate Cash Management

Good cash management practices include stewardship of cash assets to ensure collections and disbursements are managed to maximize the utility of every dollar. Cash management associated with cost shared agreements for DHHS non-MaineCare human services is currently weak.

Cash is disbursed to providers based on their budgeted (anticipated) costs rather than actual costs. DHHS makes disbursements on a regular basis (such as quarterly) regardless of when costs are actually incurred. There has historically been no systematic process for regularly adjusting scheduled disbursements if the actual costs, once realized, begin to show the budget may have been overstated.

As a result, these agreements typically end with amounts due back to the State. OPEGA reviewed recently completed cost-settlements for a sample of 28 out of 381 auditable providers⁵. We found that a majority of settlements (25, or 89%) showed money was due back to the State. The median amount owed by those providers, not including interest, was 3.4% of the total original agreement amount. The total amount providers owed for the current period settled⁶, prior to any appeals and including interest, was \$2,935,746. Nine cost-settlement audits also found the provider still owed the State from agreements settled in prior years, for an additional total owed of \$1,191,095 including interest.

Conversely, auditors determined that the State owed providers for the current period in only 5 of the 28 cost-settlement audits (18%) for a total of \$62,095. The State also still owed four providers a total of \$33,065 for prior periods. See Table 3 for a summary of cost-settlement results.

⁵ DHHS Division of Audit does not audit all providers with cost shared contracts. For example, cost settlements are not performed on providers with less than \$25,000 in cost shared contracts.

⁶ As DHHS has not been performing cost settlements until about two years after agreements end, the period settled for those in our sample was mainly State fiscal year 2004.

Table 3. Summary Results of Cost Settlements Reviewed

Settlement Status	Current Period Settlements			Prior Period Settlements		
	# of Providers	Agreement \$	Interest \$	# of Providers	Agreement \$	Interest \$
Provider Owes State	25	\$2,681,582	\$254,164	9	\$1,111,506	\$79,589
State Owes Provider	5	\$62,095	N/A ⁷	4	\$33,065	N/A

Note: Some providers from OPEGA's sample are represented in this table more than once because they both owe the State and are owed by the State.

As discussed in the Methods and Scope section of this report, our sample was not statistically random, and so can not be assumed to represent the Department's agreements in total. Nonetheless, the results of our testing suggest an opportunity to avoid distributing excess funds on cost shared agreements. Avoiding situations where providers owe substantial dollars back to the State would:

- potentially free up dollars that could be used to support other programs;
- minimize resources required for collection efforts; and
- protect providers from having to pay related interest.

Management Action:

The Department has instituted or improved some cash management controls already, and is continuing to improve others as it pursues its financial transformation strategy. The Division of Audit has been training Department program staff and the Purchased Services group to recognize funding streams for cost sharing and determine allowable costs before the agreement is finalized. Seven of these trainings were given over the past year with a total of 245 attendees.

Future actions agreed to by management are described below.

1. The Purchased Services group is developing a quarterly "true up" based on reports submitted by providers. This true-up will match agreement payments to the quarterly actual expenses and will be in place by the first quarter of FY 2009. When true-ups reveal that a provider has not expended all that they received in a quarter, DHHS staff will take appropriate action to avoid significant overpayments on the agreement. A written protocol is being developed to guide this true-up process and will be completed by FY 2010.
2. The Department is working with the DAFS Service Center on a memorandum of understanding (MOU) focused on defining roles, responsibilities, and expectations regarding cash management, grants management, and timeliness of invoicing and collections. This MOU will be in place by September 1, 2008.

⁷The State does not pay interest on amounts it owes to providers.

Finding 2 – Collection of Amounts Due Not Timely

OPEGA noted that amounts due to the State are not collected in a timely fashion, with payments being made to providers on new agreements before old receivables are resolved. As of February 2008, nine providers from our sample of 28 had not paid balances due to the State, even though the agreement periods had been closed since at least FY 2003-2004 and the cost-settlements were completed prior to November 2007. The DHHS Service Center records indicate the total amount due from providers in our sample at that time was \$1,629,524 in current and prior period balances plus interest of \$162,076. One of the providers was no longer in business, and according to DHHS' Division of Audit, \$700,897 of these balances were still under appeal and could be adjusted as a result.

Full collection of amounts due the State is hindered by the fact that DHHS has not always recorded receivables for agreements even after the agreements have had a final cost-settlement. As a result, there are some balances technically owed to the Department which have never been entered in the State's accounting system. Because of this, the total of all outstanding receivables related to cost shared non-MaineCare agreements for human services could not be determined at the time of our review. In addition, there appears to be some uncertainty about the accuracy of what has been recorded. When inquiring about how much remained due on an agreement included in our sample, OPEGA received two different answers from DHHS' Service Center and Division of Audit. One reported that the provider owed no balance, while the other reported that the State's accounting system showed a balance of over \$200,000.

Collection efforts are also complicated by the fact that many receivables are already a year or more old by the time active collection efforts begin. This time lag affects collectability. Delays in collection, or failure to collect the funds, are particularly problematic when the funds owed represent a repayment of federal funds. In these cases, DHHS may have already repaid the federal government out of the General Fund. The General Fund is, thus, not replenished unless the provider repays the State.

Although our sample was not statistically random⁸, it is reasonable to expect that uncollected amounts owed the State on cost shared agreements for human services currently exceed those in our sample. Regular recording of receivables and more assertive collection efforts would improve collection rates and timely recovery of these amounts – making more resources available for the State's use.

Management Action:

1. DHHS' Medicaid Finance group had previously been established to focus on collecting Medicaid-related receivables. The group's responsibility will now expand to include resolving past due receivables and managing collections of all DHHS agreement-related receivables. The receivables group anticipates having a complete record of all amounts owed the

⁸ The Methods and Scope section of this report has more information on the sample selection.

Department, including those well overdue, by September 30, 2008. The group will also initiate daily collection efforts for non-MaineCare agreements by the end of September, including: establishing repayment plans; noticing the debt; offset of future payments; withholding of agreements; and, withholding the next scheduled payment to a provider until the balance is paid or the provider has arranged a payment plan.

2. Beginning with agreements for fiscal year 2006, an agency must submit a check no later than 90 days after the end of the agreement period for any surplus balances identified on their final financial report. As of September 2008, the Department will begin consistently enforcing this requirement. In the event that a check is not submitted with the final report, the Department will contact and invoice the provider, thereby establishing the receivable that will be tracked and collected by the Medicaid Finance group.

Finding 3 –Improving Financial Data for Decision-Makers

Decision-makers need sound financial data to drive consideration of programmatic value and efficiency. At the beginning of our audit, DHHS' financial data for agreements was inadequate and hindered decision-making, agreement management, and oversight of the dollars spent on contracted services.

For example, we requested data showing the total budgeted versus actual costs for all DHHS agreements, but the Department was unable to provide this data. The account coding in place at that time allowed the Department to compare budget to actual for individual agreements, but not across agreements at a program or department level. When surveyed, some DHHS program managers reported that the absence of this financial data compromised their ability to accurately report on their operations and manage their funds.

The Department's new Division of Program and Fiscal Coordination has been working to address this issue since fall of 2007. They have made progress, and as of April 2008 they are now able to produce budget versus actual reports for all DHHS agreements, as well as total actual expenditure reports for all agreements cumulatively. Standard reports available to DHHS fiscal and program managers now include:

- monthly reports of agreements listed alphabetically by provider with current fiscal year encumbrances, year-to-date expenditures, and remaining balances by agreement and total for provider; and
- monthly reports of agreements by appropriation and reporting unit with current fiscal year encumbrances, year-to-date expenditures, and remaining balances by agreement and total for reporting unit and fund.

Management Action:

Additional planned improvements include the development of more detailed reports that will allow program managers to review up-to-the-minute comparisons of budget to actual for individual accounting lines within agreements. This enhanced reporting will be in place by the end of the second quarter of FY 2009.

Finding 4 – Appeals Consume Resources and May Be Avoidable

Providers appealed DHHS Division of Audit findings in 11 of the 28 cost-settlement audits we reviewed (39%). Resolution of appeals can be time consuming for both the Division of Audit and the provider involved depending on the complexity of the issue under appeal and the level of the appeal.

Despite the resources consumed, however, it appears that appeals do not typically result in significant changes to the cost-settlement findings. Audit settlements were changed in 7 of the 11 audits appealed⁹, but the changes were typically minor and totaled less than 1% (\$27,568) of the surplus amounts found due the State from the appealed cost-settlements. Interest appears more likely to be adjusted significantly, and our sample had a total of \$28,958 in interest declared no longer due as a result of appeal – a reduction of 14%. Table 4 summarizes the changes resulting from appeals in our sample.

Table 4. Summary of Results of Appeals of Cost Settlements in OPEGA's Sample

	Amount Found Due to the State	\$ Change as a Result of Appeal	% Change as a Result of Appeal
Surplus Agreement Funds	\$2,441,395	\$27,568	1%
Interest on Surplus Funds	\$213,292	\$28,958	14%

Reducing the number of appeals would free up resources in the Division of Audit, perhaps allowing cost-settlement audits to be completed more timely. It would also conserve resources and reduce costs for providers. We examined the reasons for the 31 issues raised in the 11 appealed cost-settlements and noted the following:

- 6% stemmed from provider errors in the reporting of their costs;
- 13% stemmed from Division of Audit errors;
- 23% were related to communications issues between DHHS and the provider; and
- 58% were the result of genuine disagreement between Division of Audit and the provider.

Exploring these root causes more fully could lead DHHS to establish new practices that would reduce the number of appeals. For example, most of the communication issues seemed to stem from providers receiving conflicting information from DHHS agreement managers and the Division of Audit. In a few cases, the Division of Audit reported a finding that was later appealed by the provider on the basis that Departmental program staff had written a letter or email specifically allowing the expenditure in question. Unfortunately, the communication had never reached the Division of Audit, so they had no way of knowing that the expenditure had been allowed.

⁹ Three appeals resulted in no changes and one appeal was still unresolved at the time of our review.

These situations could be avoided with better sharing of information between the Division and agreement managers. A shared network drive where all correspondence related to agreements is kept, or some other way of maintaining shared information about allowances/alterations made during the agreement's life, might be helpful. Another option would be to have the Division of Audit sign-off on an agreement allowance or adjustment before it is issued to the provider.

Management Action:

The management actions specified under Findings 1 and 2—continued training of program staff and providers, and the creation of the Division of Program and Fiscal Coordination—should help reduce the number of appeals. In addition, the DHHS Division of Audit is rewriting the Maine Uniform Accounting and Auditing Practices for Community Agencies rules. As part of this rewriting effort the Division will seek to clarify parts of the rules that are areas of frequent appeal. The rules will be rewritten by January 1, 2009.

Observation – Culture Change Critical to Successful Transformation

While DHHS management acknowledges its stewardship role, historically the Department has had a culture more focused on service delivery than adequate financial management. This imbalance resulted in an inability to connect fiscal data with program activities in an area of State government that represents 32% of the General Fund budget. Lacking this critical information hindered policy and decision-makers in their efforts to evaluate the resources being dedicated to specific programs.

DHHS recognized the need for change and is now well into a plan to transform its financial

“There is nothing more difficult to take in hand, more perilous to conduct, or more uncertain in its success than to take the lead in the introduction of a new order of things.”

Jean-Jacques Rousseau

management practices. Successful transformation, however, will require more than establishing new internal controls, reporting tools, and organizational structures. It will also require changing the underlying and long standing culture within and outside of the organization – the attitudes, perceptions and behaviors of employees at all levels and the outside stakeholder groups that influence them.

During our review, we found top management at DHHS committed to the financial transformation and able to articulate a plan and a vision. However, we also made the following observations.

- Some staff members surveyed or interviewed seemed to feel that service delivery is the primary focus of the Department and that fiscal management may interfere with that delivery rather than work in conjunction with it.

- Significant frustration exists within DHHS' staff about the clarity of roles and responsibilities and the quality of intradepartmental communications. Fourteen percent of respondents to our survey of DHHS staff involved in agreement administration indicated unclear or poorly defined roles and responsibilities hindered agreement administration and possibly caused some duplication of effort. Another thirty-six percent noted poor intradepartmental communications interfered with their productivity and made it difficult for them to quickly resolve any issues encountered.
- Management and staff described situations where political pressures and influence interfered with their ability to make decisions or take actions they felt to be in the Department's best interest.

These observations are not surprising at this point in the Department's long term transformation process. However, they do illustrate the significant challenge of the culture change that needs to occur – a challenge that can only be overcome with adequate resources, strong and consistent leadership, and active oversight and support of the Executive and Legislative branches.

Agency Response

In accordance with 3 MRSA §996, OPEGA provided the Department of Health and Human Services an opportunity to submit comments on the draft of this report. The response letter can be found at the end of this report.

Acknowledgements

OPEGA would like to thank the management and staff of the Department of Health and Human Services and the DHHS Service Center who worked with us throughout this audit. Their cooperation and willingness to share their time and knowledge was appreciated.

APPENDICES

Appendix A. Statutory Definitions Pertaining to Contracting with Community Based Agencies

34-B §1208. Agreements with community agencies

1. Definitions. As used in this section, unless the context indicates otherwise, the following terms have the following meanings.

A. "Agreement" means a legally binding document between 2 parties, including documents commonly referred to as accepted application, proposal, prospectus, contract, grant, joint or cooperative agreement, purchase of service or state aid. [1983, c. 459, §7 (NEW) .]

B. "Community agency" means a person, a public or private nonprofit organization or a firm, partnership or business corporation operated for profit, which operates a human service program at the community level. [1983, c. 459, §7 (NEW) .]

C. "Funds" means any and all general funds, dedicated funds, fees, special revenue funds, 3rd party reimbursements, provider payments or other funds available for expenditure by the department in support of the provision of a human service. [1983, c. 459, §7 (NEW) .]

D. "Human service" means any alcoholism, children's community action, corrections, criminal justice, developmental disability, donated food, education, elderly, food stamp, income maintenance, health, juvenile, law enforcement, legal, medical care, mental health, mental retardation, poverty, public assistance, rehabilitation, social, substance abuse, transportation, welfare or youth service operated by a community agency under an agreement financially supporting the service, wholly or in part, by funds authorized for expenditure by the department. [1983, c. 459, §7 (NEW) .]

E. "Nonprofit organization" means any agency, institution or organization which is, or is owned and operated by, one or more corporations or associations, no part of the net earnings of which inures, or may lawfully inure, to the benefit of any private shareholder or individual and which has a territory of operations that may extend to a neighborhood, community, region or the State. [1983, c. 459, §7 (NEW) .]

F. "Public" means municipal, county and other governmental bodies which are political subdivisions within the State. [1983, c. 459, §7 (NEW) .]

G. "State agency client" has the same meaning as in Title 20-A, section 1, subsection 34-A. [1985, c. 789, §§7, 9 (NEW) .]

H. "Service provider" means a community agency providing services for children with mental health needs, mental retardation and autism. [2003, c. 673, Pt. SSS, §1 (NEW) .]

[2003, c. 673, Pt. SSS, §1 (AMD) .]

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Appendix B. Interim Fiscal Opportunity Memo to Government Oversight Committee

To: Senator Elizabeth Mitchell, Senate Chair
Representative Marilyn Canavan, House Chair
Members of the Government Oversight Committee

From: Beth Ashcroft, Director of OPEGA

Date: February 27, 2008

Re: Fiscal Opportunities Related to Contracting for Health and Human Services

OPEGA is currently conducting a performance audit of contracting for health and human services in the Department of Health and Human Services (DHHS). We have identified some fiscal opportunities in connection with our work to date. Normally, we would wait to make you aware of these opportunities and related issues until we had completed our work and issued our final report. Given the State's serious financial circumstances, however, we are honoring your request to communicate any potential savings ideas as soon as possible in hopes they may be helpful as the Legislature works through the supplemental budget.

This memo briefly discusses two fiscal opportunities related to non-Medicaid cost-settled contracts for social services. Should the Legislature decide to pursue these opportunities, we expect the ensuing legislative process will allow for a more thorough exploration of each idea and the appropriate involvement of DHHS and other stakeholders. These opportunities do not represent the entirety of OPEGA's work on the audit of DHHS contracting nor all the issues that may be included in the audit's eventual final report.

Background

DHHS contracts for some social services using a cost sharing arrangement. In such an arrangement, DHHS agrees to cover a certain percentage of the provider's costs for expenses allowed under the contract's guidelines or applicable federal regulations. At the beginning of the contract period, the provider presents a proposed budget from which the amount DHHS expects to contribute is calculated. That amount is then paid out to the provider in pre-determined periodic installments over the course of the contract period with adjustments for unplanned but allowable expenses made as necessary. At the end of the contract period, the provider submits statements which show actual costs for allowable expenses and payments received from DHHS. This statement also indicates whether the provider has received more than needed, or not enough, during the contract period.

Each cost sharing contract eventually goes through a formal and final cost-settlement process conducted by auditors in DHHS' Division of Audit. During this process, auditors confirm that the actual expenses submitted by the provider for cost sharing are allowable. They then reconcile the actual allowable amounts to payments made to the provider and come to a final determination on any amount due from the provider to the State or vice versa. The auditors also

calculate interest on amounts due as appropriate. Providers may elect to contest the auditors' findings through an established appeals process in DHHS.

Fiscal Opportunities

1. Payments to Providers During the Contract Period

We reviewed the cost-settlements for a sample of 28 providers with social service contracts. Many of the providers had multiple cost sharing contracts which were all cost-settled by the Division of Audit at the same time. In a majority of these cost-settlement audits (25 or 89%), the auditor determined the provider owed the State money on one or more contracts. The total amount providers owed, prior to any appeals, was \$2,681,582 plus related interest of \$254,164. The median amount owed by those providers, not including interest, was 3.4% of the total amount of the original contract(s). Nine of the cost-settlement audits also found that the provider still owed the State from contract periods that had been settled in prior years. The total amount providers owed from prior years was \$1,111,506 plus interest of \$79,589. Conversely, auditors determined that the State owed providers in only 5 of the 28 cost-settlement audits (18%) for a total of \$62,095 in the current period and \$33,065 for prior periods.

Our sample was not statistically random, and so can not be assumed to represent the Department's contracts in total. Nonetheless, these results suggest that there may be opportunity to avoid distributing as much money on cost sharing contracts in the first place. Avoiding situations where providers owe substantial dollars back to the State would:

- potentially free up dollars that could be used to support other programs;
- minimize issues related to collection of these amounts; and
- protect providers from having to pay related interest.

2. Collection of Amounts Due the State

DHHS is currently cost-settling contracts about 2 years after the contracts have ended. DHHS' accounting service center is then charged with attempting to account for, and collect, receivables that are only recently realized, but are actually a few years old. This time lag affects collectability and it does appear that providers are not repaying amounts due the State in a timely fashion. For various reasons, providers sometimes have difficulty repaying balances due so long after the contract has ended.

Delays in collection, or failure to collect the funds, are particularly problematic when the funds owed represent a repayment of federal funds. In these cases, DHHS may have already repaid the federal government out of the General Fund. The General Fund is, thus, not replenished unless, or until, the provider repays the State.

At present, 9 providers from our sample have yet to repay amounts due the State, even though the contract periods have been closed since at least FY 2003-2004 and the cost-settlements were completed prior to November 2007. The DHHS Service Center's records indicate the total amount currently due from providers on cost-settlements in our sample is \$1,610,725 in current and prior period balances plus interest of \$161,200. One of the

providers is no longer in business, and according to DHHS' Division of Audit, \$700,897 of these balances are still under appeal and could be adjusted as a result.

As previously noted, our sample was not statistically random, and so can not be assumed to represent the Department's contracts in total. Still it is reasonable to expect that amounts owed the State on cost sharing contracts for social services currently exceed those in our sample. If providers are incapable of making full and immediate repayment, DHHS could explore alternatives such as repayment plans or reducing upcoming payments to providers by the amounts due.

The State's fiscal situation could also be improved by reducing the time lags in completing cost-settlements. This, however, would likely require additional audit resources. Being more proactive in collecting amounts due prior to cost-settlement is another option for improving cash flow within DHHS and the collectability of amounts due.

Department Response

We have discussed the contents of this memo with the Department of Health and Human Services. Their written response is attached.

Department of Health and Human Services
 Response to OPEGA's report "Fiscal Opportunities Related to DHHS Contracting"
 February 27, 2008

The Department recognizes the benefit of limiting the pre-payment of contracts and avoiding overpaying of the contracts which leads to a receivable from the Community Agency once the contract period has ended. In an effort to minimize both situations, the Department has improved training opportunities and has implemented or improved several controls.

1. The Division of Audit is training Department program staff and the contract services group. Staff now recognizes funding streams for cost sharing and determine allowable vs. unallowable costs before the contract is finalized.
2. The Division of Audit has provided several trainings on cost sharing which leads to more accurate filings by the Community Agencies.

The results are approved contracts that exclude unallowable costs up front and a clearer understanding of the final settlement calculated by the Community Agency at the contract's end. This ensures that contracted funds are used appropriately.

3. The Division of Purchased Services is developing a quarterly "true up" based on the quarterly submission of reports from Community Agencies. This matches contract payments to the quarterly actual expenses.

The Department also recognizes the importance of appropriately recording receivables as well as improving the timeliness of collecting receivables established through the agreement close-out process. The Department has instituted or improved controls and is continuing to work to improve the collections process.

4. An agency must submit a check for any surplus balances identified on their final financial report which is due to the Department no later than 90 days after the end of the agreement period. Rather than "truing up" at the time of cost settlements, this payment requirement has been added to contracts starting in 2006. The Department has recognized timelier collections as a result of this change.
5. In the event that a check is not submitted with final report, the Department will contact and invoice the Community Agency, thereby establishing the receivable that will be tracked and collected by the Receivables group.

The Department is working toward an accounts receivable group responsible for the collection of all amounts due the Department. Currently the focus of the group is Medicaid-related receivables; however, this group will be expanding their collection efforts to include recoveries of contract settlements, program integrity recoupments, and other receivables due the Department.

Department of Health and Human Services
Response to OPEGA's report "Fiscal Opportunities Related to DHHS Contracting"
February 27, 2008
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6. Daily collection efforts throughout the Department include:
 - Establishing repayment plans;
 - Noticing the debt;
 - Offset of future payments;
 - Withholding of contracts;
 - Withholding the next scheduled payment to an Agency until the balance is paid or the Agency has made arrangements for payment plan.

The Department recognizes the need to balance its fiscal management responsibilities with ensuring the continuation of vital services Maine people.

Finally, it should be noted that while these efforts will help improve cash flow, the collection of these funds does not necessarily represent a savings initiative. Much of the overpayments identified in OPEGA's report are already built into the baseline budget assumptions of the Department.



*Department of Health
and Human Services*

*Maine People Living
Safe, Healthy and Productive Lives*

John E. Baldacci, Governor

Brenda M. Harvey, Commissioner

Department of Health and Human Services
Commissioner's Office
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TTY: 1-800-606-0215

July 7, 2008

Beth Ashcroft, Director
OPEGA
#115 State House Station
Augusta, ME 04333-0115

Dear Ms. Ashcroft:

The Department appreciates the manner in which OPEGA conducted its performance audit, providing executive management with several opportunities to respond to its findings, offer context, and add supplemental information. The report validates the financial management issues the Department had previously identified, and we welcome the opportunity to present this brief update on the significant progress already made.

The Department continues to pursue a comprehensive restructuring in the management of its financial affairs. For example, the creation of a new Division of Program and Fiscal Coordination, and the reorganization of the Rate Setting Unit and the Division of Purchased Services under the umbrella of the Deputy Commissioner for Finance are complete. The design provides for a more integrated balance between the delivery of social services and management of the resources required to provide them.

By connecting the contracting, accounting and audit functions, the Department has strengthened internal controls, increased training opportunities, and enhanced its communication with community service agencies. Clearer understanding has led to an improved recognition of funding streams available for cost sharing and the determination of allowable costs – before a contract is executed.

Community agencies have responded by filing more accurate quarterly compliance reports. The Division of Purchased Services has developed a quarterly “true up” using these reports to match contract payments with actual expenses and to take steps, if necessary, to ensure that significant overpayment on an agreement is avoided.

Perhaps the greatest shift in organizational culture began with the addition of Program Fiscal Coordinators in each Office. As more and better financial reporting tools are made available, increased transparency and accountability has occurred. Managers at all levels are pleased with the results and have responded well to the changes. The Department recognizes the

Beth Ashcroft, Director
July 7, 2008
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need to balance its fiscal management responsibilities with ensuring the continuation of vital services to Maine people.

The most significant efforts currently underway are in the area of cash management.

DHHS has established an Accounts Receivable group charged with collecting amounts due to the Department. The group has focused primarily on Medicaid-related receivables in the past. Their charge has been expanded, however, to include recoveries from settled contracts, program integrity, and any other receivables due the Department. Routine collection efforts include: the noticing of debt, establishing repayment plans, with-holding new contract awards, making offsets to current payments, and holding scheduled future payments in abeyance until an outstanding obligation is satisfied or some other arrangement has been made.

The track record of the Medicaid finance team in managing large and complex collections endeavor is noteworthy. Over \$500 million has been recovered, which represents 90% of interim overpayments caused by well-documented issues with the MeCMS claims processing system. This indicates that by applying the lessons learned, and by leveraging the systems and processes developed in managing that effort, the group is capable of collecting on amounts due the Department resulting from the agreement closeout process.

Please note that while this effort will increase cash flow, collection of these obligations does not necessarily represent a budget savings initiative, since most of the overpayments identified in the OPEGA report are already included in the baseline budget assumptions of the Department.

In partnership with the DAFS Service Center and the Office of the State Controller, new payables processes are being developed to improve accuracy and timeliness through better matching of payment obligations with available funds.

An on-going challenge has been the limited number of people available to do the work. The Department gratefully acknowledges and very much appreciates the funding provided by the Legislature to create ten new positions in the Service Center who will be deployed to help implement the Department's improvement plan. However, the recent loss of a key Department leader in the drive to improve financial results, the Deputy Commissioner for Finance, poses an additional risk. We will, however, remain vigilant about our staffing and financial management.

Sincerely,

A handwritten signature in black ink that reads "Brenda Harvey". The signature is written in a cursive, flowing style.

Brenda M. Harvey
Commissioner

BMH/klv